

# Improving housing affordability through tax reform

## Australia and the UK in comparison

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# The Henry Review recommendations

## Stamp duty and land tax

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# Introduction

- There are two main recommendations from the Henry Review on tax reform:
  - Stamp duties on conveyance to be abolished and replaced by a broad based land tax that is paid by landowners and levied by applying a progressive rate structure to m<sup>2</sup> land values and land size.
  - A savings income discount (SID) of 40% will apply to the net rental income (including capital gains) from most non-business assets.
- The number of taxes is reduced by one as there is already a land tax.

# Introduction

- Today's presentation will concentrate on the first of these recommendations.
- We begin by using economic analysis to predict impacts within land and housing markets.
- Some empirical estimates of likely incidence are then presented.
- We conclude by drawing out implications for housing affordability and urban land use.

# Stamp duties

## Why abolish them?

- There is no strong efficiency rationale.
- The duty does not achieve an obvious redistribution goal.
- Stamp duties can impede access to home ownership, and deter investment in rental housing.
- Those who move more frequently pay relatively high amounts of duty during their lifetimes.
- It deters the transfer of property from lower value uses to higher value uses. It therefore impedes the efficient allocation of land and buildings between competing uses.
- But an important (if volatile) source of tax revenue for state governments.

# Present land tax arrangements

## The case for reform

- Land tax is distortionary because land used for owner occupied housing (and primary production) is tax exempt, while land used for private rental housing (and commercial or industrial uses) is taxed.
- Land tax applies to the cumulative unimproved value of land:
  - Single property owners typically have a small or more often zero tax liability, while multiple property owners have relatively high tax burdens.
- Important implications for affordable rental housing supply:
  - Contraction in the supply of rental housing.
  - Important barrier to the attraction of private finance (superannuation funds, for instance).

# Recommended land tax arrangements

## Rationale

- If no land is exempt, taxes will be capitalised into lower land values.
- Landowners cannot 'escape' the tax by changing land use.
- The supply of rental housing will expand.
- But if (say) land for primary production is exempt, urban land use will contract.
- Cities will be more compact with higher population densities.
- But the neutrality benefits of a broad based land tax are lost.

# Empirical analysis

## How much will land owners pay under reforms?

- Two main data sources
  - property valuations data
  - property sales data.
- Land plots and property sales geocoded - allows important analyses of the spatial incidence of taxes and duties.
- The valuation records of up to 1 136 000 residential land plots in Melbourne municipalities are used for the analysis of land tax.
- The final sample for analysis of stamp duties within metropolitan Melbourne, amount to around 68 400 transaction records.

# Empirical analysis

## How much will land owners pay under reforms?

- The reformed land tax schedule has been designed such that it has a progressive rate structure; the rate increases with the m<sup>2</sup> dollar value of land.
- The rates of land tax and thresholds are set such that the reforms are revenue neutral (exactly compensate for the loss of \$1.3b of stamp duty revenue).
- We assume that there will be seven land tax brackets under the new land tax system, exactly the same number of tax brackets as under the current (2006) land tax system.

# Descriptive statistics

## Proposed land tax schedule and average annual land tax payments

Land tax bracket	Number of land plots	Marginal Tax Rate (%)	Average annual land tax (\$)
Less than \$286.54	305,163	0%	0.00
\$286.54 to less than \$974.45	593,907	0.786%	1,114
\$974.45 to less than \$2000.22	104,152	0.876%	4,147
\$2000.22 to less than \$3025.30	19,197	0.966%	5,706
\$3025.30 to less than \$4145.28	6,907	1.056%	6,971
\$4145.28 to less than \$5697.08	3,075	1.146%	8,224
\$5697.08 and over	790	1.236%	18,041
Overall average annual land tax			7,367

# Descriptive statistics

## Land value by distance from CBD (10km)

Distance from CBD	Number of residential land plots (thousands)	Total residential land area (million m <sup>2</sup> )	Mean land value (\$ per m <sup>2</sup> )	Mean land value (\$'000 per land plot)
0km < 10km	174	89	1,335	551
10km < 20km	348	238	553	365
20km < 30km	240	179	377	258
30km < 40km	131	107	278	196
40km < 50km	72	65	309	246
50km < 60km	29	27	295	238
60km < 70km	37	36	310	272
> 70km	3	3	318	320
Total	1,033	744	576	335

# Simulation modeling and spatial analysis

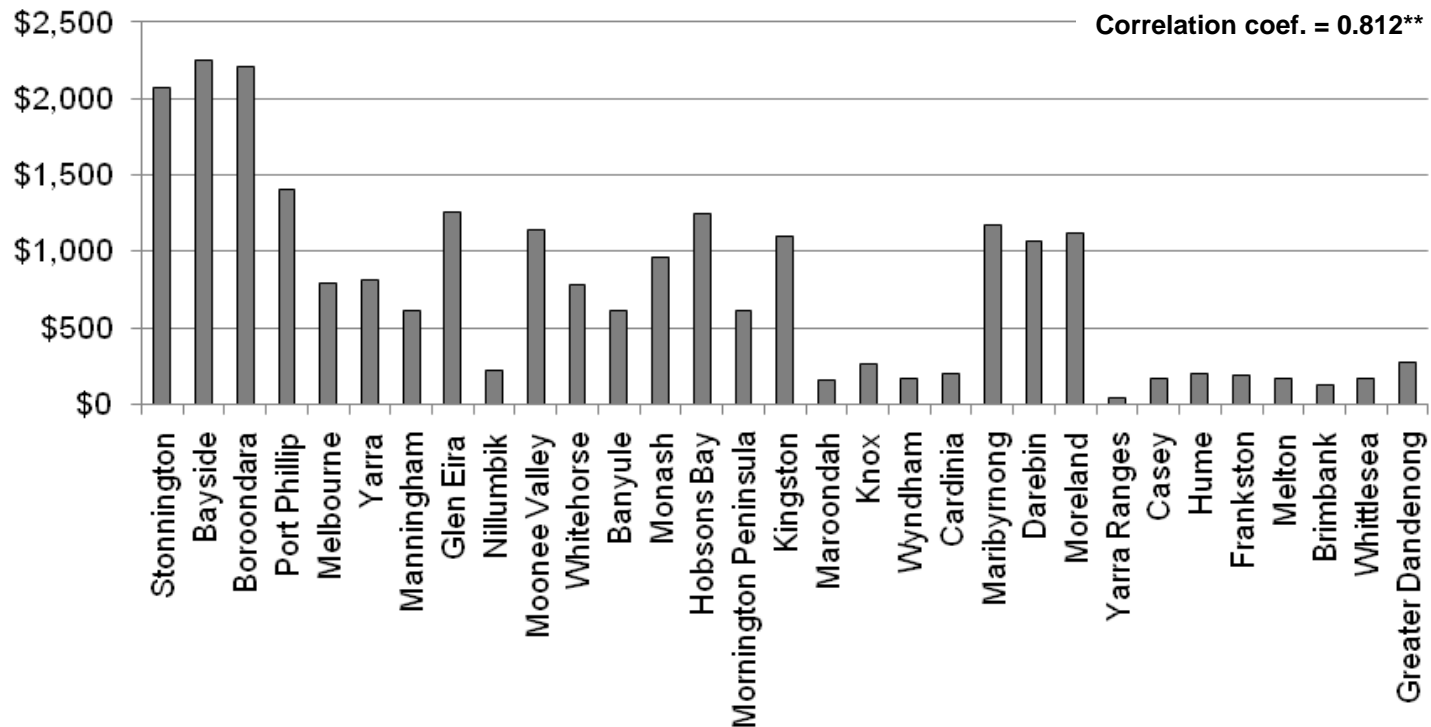
## Proposed land tax and distance from CBD (10km rings)

Distance to CBD (10km intervals)	Proposed land tax				
	Revenue			Total Land Area <i>m<sup>2</sup> (millions)</i>	Mean Land Value <i>\$ per m<sup>2</sup></i>
	Sum \$ ( <i>millions</i> )	% of Aggregate revenue	Average <u>RATE</u> of land tax		
<b>0km &lt; 10km</b>	590	46%	0.6%	89	1,335
<b>10km &lt; 20km</b>	488	38%	0.4%	238	553
<b>20km &lt; 30km</b>	130	10%	0.2%	179	377
<b>30km &lt; 40km</b>	29	2%	0.1%	107	278
<b>40km &lt; 50km</b>	25	2%	0.1%	65	309
<b>50km &lt; 60km</b>	10	1%	0.2%	27	295
<b>60km &lt; 70km</b>	17	1%	0.2%	36	310
<b>➤70km</b>	2	0.2%	0.2%	3	318
<b>Total</b>	1,290		0.4%	744	576

# Simulation modeling and spatial analysis

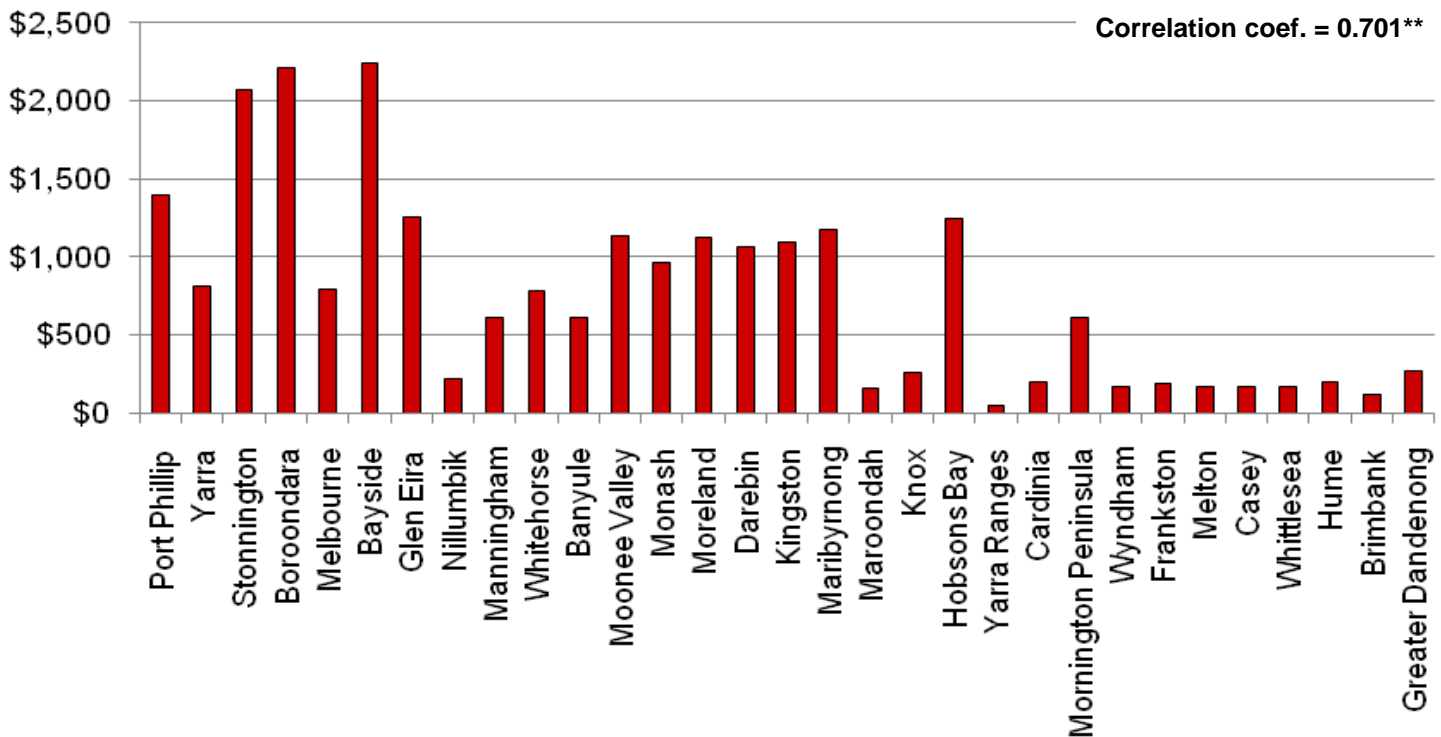
## Annual land tax per taxpayer by socio-economic indicators

Municipalities ranked from highest to lowest in terms of taxable income per taxpayer



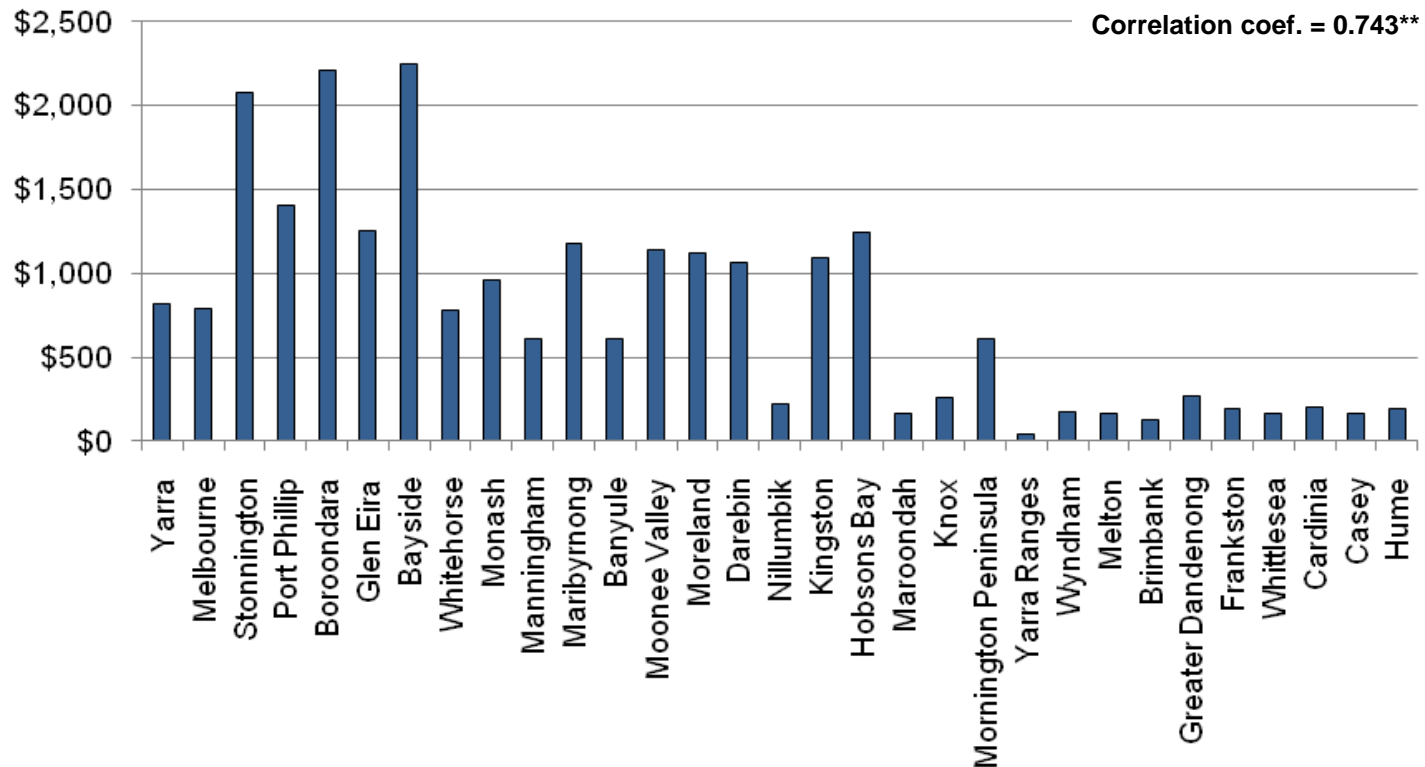
# Simulation modeling and spatial analysis

Municipalities ranked from highest to lowest in terms of proportion of residents who are managers or professionals



# Simulation modeling and spatial analysis

Municipalities ranked from highest to lowest in terms of proportion of residents with bachelor degree or higher



# Simulation modeling and spatial analysis

Average rates of land tax and stamp duty, by land value per m<sup>2</sup> (deciles)

Land value deciles	Proposed land tax schedule				Stamp duty			
	Revenue			Mean land value \$ per m <sup>2</sup>	Revenue			Mean property value \$'000s
	Sum \$(millions)	% of Aggregate Revenue	Average <u>RATE</u> of Land Tax		Sum \$(millions)	% of Aggregate Revenue	Average <u>RATE</u> of Stamp Duty	
1	0	0%	0.03%	154	19	1%	2.5%	114
2	0	0%	0.02%	226	39	3%	3.4%	167
3	0 <sup>a</sup>	0% <sup>a</sup>	0.1%	268	60	5%	4.0%	218
4	13	1%	0.1%	310	79	6%	4.3%	254
5	41	3%	0.2%	361	84	7%	4.5%	288
6	80	6%	0.3%	433	105	8%	4.7%	328
7	132	10%	0.3%	530	124	10%	4.9%	379
8	197	15%	0.4%	665	153	12%	5.0%	447
9	305	24%	0.5%	912	206	16%	5.2%	574
10	522	40%	0.6%	1,898	420	33%	5.5%	1,124
<b>Total</b>	1,290		0.4%	576	1,290		4.9%	389

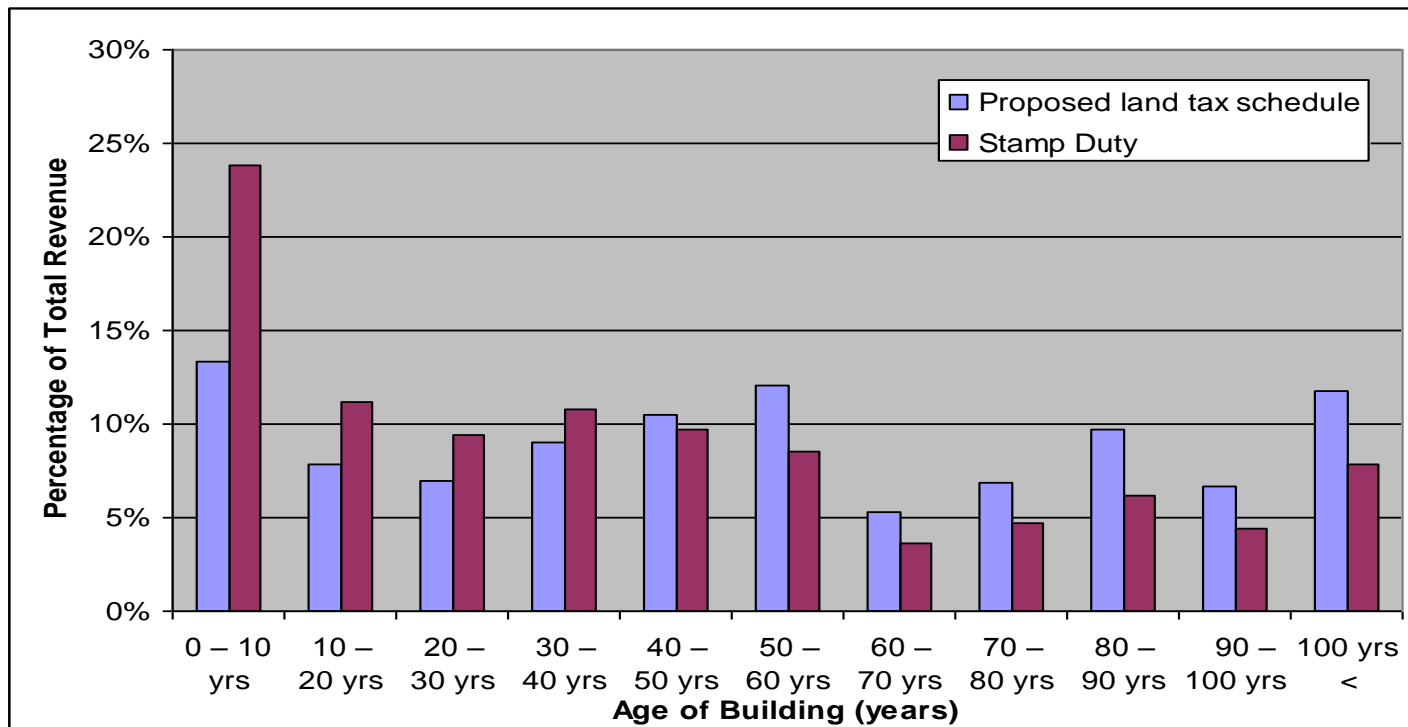
# Simulation modeling and spatial analysis

Average rate of land tax, by land area (quintiles)

<b>Proposed Land Tax Schedule</b>				
Land Area <i>m</i> <sup>2</sup>	Revenue			Mean Land Tax Liability \$ per <i>m</i> <sup>2</sup>
	Sum \$ ( <i>millions</i> )	% of Aggregate Revenue	Average <u>RATE</u> of Land Tax	
<b>124 &lt; 533</b>	411	32%	1%	6.9
<b>534 &lt; 608</b>	200	16%	0.3%	1.7
<b>609 &lt; 688</b>	227	18%	0.4%	1.7
<b>689 &lt; 821</b>	243	19%	0.3%	1.6
<b>822 &lt;</b>	209	16%	0.3%	1.0
<b>Total</b>	1,290		0.4%	2.6

# Simulation modeling and spatial analysis

Percentage of total revenue from proposed land tax and stamp duty, by age of building



# Simulation modeling and spatial analysis

Reduction in mean land values due to the proposed land tax, by distance from CBD (10km ring)

<b>Distance from CBD (10km ring)</b>	<b>Mean Assessed Land Value \$</b>	<b>Mean Reduction in Land Value due to Capitalisation \$</b>	<b>% Decrease in Mean Land Value after Capitalisation</b>
<b>0km &lt; 10km</b>	551,099	56,425	10%
<b>10km &lt; 20km</b>	365,163	23,408	6%
<b>20km &lt; 30km</b>	257,852	9,018	3%
<b>30km &lt; 40km</b>	196,434	3,697	2%
<b>40km &lt; 50km</b>	245,891	5,714	2%
<b>50km &lt; 60km</b>	238,185	5,956	3%
<b>60km &lt; 70km</b>	271,739	7,654	3%
<b>≥ 70km</b>	319,904	12,633	4%
<b>Total</b>	<b>334,877</b>	<b>20,822</b>	<b>6%</b>

# Key findings and implications

- The Henry Review Land Tax Recommendations will radically redistribute tax burden.
- Smaller land plots closer to the CBD will have higher tax burdens.
- Land tax burdens will be higher in communities with higher incomes.
- Capitalisation effects will lower land and property values in those areas of cities where pressure on land and property markets has been greatest.

# Key findings and implications

- The supply of rental housing will be boosted by the reforms
- Because the recommended land tax is applied at rates that increase with per m<sup>2</sup>
  - We can expect some relocation away from the central cities,
  - And if a zero threshold is designed to exempt rural land, cities will be more compact than would otherwise be the case

# Land tax and the Savings Income Discount

- Negatively geared investors find that tax shelter benefits are curbed by the Savings Income Discount.
- But the land tax reforms will offer some relief because their land tax payments will be lower than under current arrangements.